SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

ACA FINANCIAL GUARANTY CORP.,

Plaintiff,

v.

GOLDMAN, SACHS & CO., PAULSON & CO., INC. and PAULSON CREDIT OPPORTUNITIES MASTER II, LTD.,

Defendants.

Index No. 650027/2011
(Kapnick, J.)
Date Purchased: 1/6/2011

Date Supplemental Summons Filed:

(E-File Case)

SUPPLEMENTAL SUMMONS

Plaintiff designates New York County as the place of trial.

Venue is based on Plaintiff's Principal Place of Business:

600 Fifth Ave., New York, N.Y. 10020

TO THE ABOVE-NAMED DEFENDANTS PAULSON & CO., INC. and PAULSON CREDIT OPPORTUNITIES MASTER II, LTD.:

You are hereby summoned to answer the Second Amended Complaint in this action and to serve a copy of your answer on the Plaintiff's Attorneys within twenty (20) days after the service of this summons, exclusive of the day of service (or within thirty (30) days after the service is complete if this summons is not personally delivered to you within the State of New York); and in case of your failure to answer, judgment will be taken against you by default for the relief demanded in the complaint.

Dated: New York, New York
January _, 2013

KASOWITZ, BENSON, TORRES &
FRIEDMAN LLP

By: _____

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TO: Paulson & Co., Inc. and
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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

ACA FINANCIAL GUARANTY CORP.,	:	
	:	Index No.
Plaintiff,	:	650027/2011
	:	
- against -	:	
	:	**SECOND AMENDED**
	:	**COMPLAINT**
GOLDMAN, SACHS & CO., PAULSON & CO., INC., PAULSON CREDIT OPPORTUNITIES MASTER II, LTD,	:	
Defendants.	:	

Plaintiff ACA FINANCIAL GUARANTY CORPORATION ("ACA"), for its complaint against defendant GOLDMAN, SACHS & CO. ("Goldman Sachs"), PAULSON & CO., INC. ("Paulson & Co") and PAULSON CREDIT OPPORTUNITIES MASTER II, LTD. ("Paulson Credit Opportunities," and together with Paulson & Co, "Paulson"), alleges as follows:

Preliminary Statement

1. This fraud action arises from the egregious conduct of Goldman Sachs, a prominent investment bank, and its hedge fund client Paulson, in conceiving and marketing a structured finance product -- based on a portfolio of investment securities selected largely by Paulson -- which was designed to fail so that Paulson could reap huge profits by shorting the portfolio and Goldman Sachs could reap huge fees. Goldman Sachs and Paulson conspired to fraudulently induce ACA, a monoline bond insurance company now operating in run-off, to provide financial guaranty insurance for that structured finance product. Goldman Sachs and Paulson did so by deceiving ACA into believing that Paulson was to be the "equity" investor -- *i.e.*, a long investor -- in that

product, a synthetic collateralized debt obligation Goldman Sachs called ABACUS 2007-AC1 ("ABACUS"). In fact, as Goldman Sachs and Paulson knew, Paulson intended to take an enormous short position in ABACUS, thereby taking an economic position in the transaction precisely contrary to ACA's position as insurer.

2. Had Paulson's true role as a short investor selecting the portfolio been known, neither ACA nor anyone else would have provided financial guaranty insurance for ABACUS. Because of Goldman Sachs and Paulson's deceit -- which led ACA to reasonably believe that ABACUS was a valuable product selected largely by the equity investor -- ACA insured a financial product that was doomed to fail.

3. To effectuate their scheme, Goldman Sachs fraudulently misrepresented to ACA that, among other things, Paulson, as the purported "transaction sponsor," had "pre-committed" to invest in the equity of ABACUS, and that the economic interest of Paulson and ACA in ABACUS were, therefore, "aligned," and Paulson, using what Paulson itself has admitted was a previously-employed and well-rehearsed "script," fraudulently "play[ed] the role" of the "equity investor" in ABACUS. Indeed, the audio recording of a telephone conversation between ACA and a Goldman Sachs Managing Director records Goldman Sachs expressly and unequivocally misrepresenting to ACA that Paulson's economic interest in the "capital structure" of ABACUS was "100% equity." Not only did Goldman Sachs and Paulson deceive ACA into believing that Paulson was to be the "equity" investor in ABACUS, Goldman Sachs and Paulson also secretly agreed to structure the transaction in a manner -- through what they called a "Side Letter Agreement" -- that concealed Paulson's short interest in ABACUS.

4. Goldman Sachs engaged in this egregious misconduct notwithstanding that it expressly acknowledged that its participation presented "reputational risk" and after at least one other major investment bank declined to participate for that very reason. Goldman Sachs has since settled SEC civil charges arising out of this fraudulent conduct, agreeing to pay a $550 million fine.

5. Citing ABACUS as a prominent example of Goldman Sachs's contribution to causing the recent financial crisis, the United States Senate Permanent Subcommittee on Investigations (the "Subcommittee") concluded after an 18-month investigation that Goldman Sachs was one of the "self-interested promoters of risky and complicated financial schemes that helped trigger the crisis." With respect to ABACUS in particular, the Subcommittee concluded that Goldman Sachs knew that Paulson would "profit only if [ABACUS] lost value," yet allowed Paulson to "play a major role in selecting the assets" while failing to disclose Paulson's true "investment objective."

6. ACA, one of the principal victims of Goldman Sachs and Paulson's fraudulent scheme, brings this action to recover over $30 million in compensatory damages -- the losses proximately caused by Goldman Sachs and Paulson's misconduct -- and $90 million in punitive damages.

Jurisdiction And Venue

7. This Court has personal jurisdiction over defendants pursuant to CPLR § 301, as they are domiciled in New York State, or pursuant to CPLR § 302, in as much as the causes of action asserted herein arise from defendants' (i) transacting business in New York State, (ii) having committed a tortious act within New York State,

and/or (iii) having committed a tortious act without New York State causing injury to property within New York State.

8. Venue is proper pursuant to CPLR § 503, as one or more parties reside in New York County.

The Parties

9. Plaintiff ACA, a Maryland stock insurance corporation, is a monoline bond insurer headquartered at 600 Fifth Avenue, New York, New York. Pursuant to a restructuring plan approved by the Maryland Insurance Administration on or about August 8, 2008, ACA operates as a run-off financial guaranty insurance company with the sole business purpose of honoring valid claims for the timely payment of interest and ultimate payment of principal on municipal and other public finance bonds that ACA guaranties.

10. Defendant Goldman Sachs, a registered U.S. broker-dealer, is a limited partnership formed under the laws of the State of New York, with its head office in New York, New York.

11. Defendant Paulson & Co. is an investment advisor registered under the Investment Advisors Act of 1940 and incorporated under the laws of the State of Delaware, with its principal office in New York, New York. As the investment manager of Paulson Credit Opportunities, Paulson & Co. acted as its agent in connection with ABACUS.

12. Defendant Paulson Credit Opportunities is a hedge fund incorporated under the laws of the State of Delaware with its principal office in New York, New York.

Facts

I. Background

A. The Nature of the Financial Instruments at Issue

13. In late 2006, Paulson approached Goldman Sachs seeking a way to take a massive short position on subprime residential mortgage backed securities ("RMBS"), which are essentially pools of residential mortgages that have been repackaged into bonds. ABACUS was a synthetic collateralized debt obligation ("CDO") referencing a portfolio of RMBS, which enabled Paulson to do precisely that.

14. A CDO is an asset-backed security based on a portfolio of fixed-income collateral, such as RMBS. To establish a CDO, an investment bank incorporates a special purpose vehicle to which equity investors contribute capital. The special purpose vehicle raises additional capital by issuing notes and is, therefore, commonly referred to as the "Issuer." In the most common type of CDO, known as a "cash flow" CDO, the Issuer uses the proceeds of the notes to purchase collateral and makes payments on the notes out of the cash flow generated by the collateral. As explained further below, ABACUS was not a cash flow CDO but a "synthetic" CDO.

15. The notes are divided into different classes of risk, known as "tranches." Payments on the notes are made in order of seniority. Thus, notes in the most senior tranche -- the so-called "super senior" tranche -- are paid first, while notes in more junior tranches are paid only after all senior notes have been paid in full. As a result, senior notes have the lowest risk that they will not be paid due to defaults in the underlying portfolio. However, senior notes also bear the lowest interest rate. Conversely, more

junior notes have a higher risk that they will not be paid, but they bear a higher interest rate relative to the senior notes.

16. Equity investors in a CDO are in the lowest tranche of the capital structure. They are the first to suffer losses attributable to defaults on the underlying collateral. Thus, the equity tranche is often referred to as the "first loss" tranche. While equity investors have the highest potential rate of return, they also have the highest risk of loss.

17. CDOs are frequently "wrapped" -- that is, a financial guaranty insurer (such as ACA) issues an insurance policy unconditionally guarantying payment of senior notes in or above a specified tranche in the capital structure, known as the "attachment point." Thus, the financial guaranty insurer suffers losses only if the equity investment and all notes beneath the attachment point are wiped out. Such a financial guaranty policy for the most senior portion of the capital structure is referred to as a "super senior wrap."

18. A credit default swap ("CDS") is an over-the-counter (*i.e.*, not traded on a formal exchange) derivative contract referencing a bond or other financial obligation (the "reference obligation"). The parties to a CDS are referred to as the protection buyer and the protection seller. The protection buyer makes fixed periodic payments, commonly referred to as premiums, to the protection seller. In exchange, the protection seller agrees to make a "contingent payment" to the protection buyer if the reference obligation experiences a defined credit event, such as a default. The contingent payment is typically orders of magnitude larger than the premium payments.

19. When the protection buyer owns the reference obligation, the CDS functions like an insurance policy in the sense that any losses from a default of the reference obligation will be offset by gains on the CDS. In a "naked" CDS, the protection buyer does not own the reference obligation, in which case the protection buyer positions itself to profit from a default of the reference obligation -- similar to insuring another person's residence in the expectation that it will be destroyed by a fire -- because the protection buyer will get a large contingent payment. In either event, the protection seller takes the "long" position -- meaning it takes the position that the reference obligation will perform -- and the protection buyer takes the "short" position -- meaning it takes the position that the reference obligation will default.

20. A synthetic CDO -- such as ABACUS -- combines a CDO and CDSs. The Issuer does not purchase a portfolio of collateral but instead acts as the protection seller in one or more CDSs referencing a portfolio of collateral (the "reference portfolio"). Like a cash flow CDO, a synthetic CDO may also issue notes on which it pays principal and interest. However, a synthetic CDO generates cash flow to pay the notes from the premiums it receives from the protection buyer, not from income generated by the collateral itself. The Issuer invests the proceeds from the sale of the notes in low-risk securities, which it uses to make contingent payments arising from defaults in the reference portfolio.

21. Synthetic CDOs are structured so that long investors can participate in the capital structure by purchasing notes or, unlike cash CDOs, by selling protection on a specified tranche of the capital structure. Thus, synthetic CDOs do not necessarily issue notes for every tranche in the capital structure. In the parlance of the financial industry, a

synthetic CDO that does not issue notes for every tranche in the capital structure is "not fully distributed." Whether an investor purchases notes in or sells protection on a tranche, the investor's exposure to the risk of default in the underlying portfolio is the same.

22. In sum, a synthetic CDO is a mechanism to profit on a massive scale from the failure of the collateral specified in the reference portfolio. The protection sellers, including the financial guarantor of the super senior tranche of the capital structure, and the noteholders take the long position -- meaning they both take the position that the reference portfolio will perform -- while the protection buyers take the short position -- meaning they take the position that the reference portfolio will default.

B. The Role of Investment Banks, Transaction Sponsors and Portfolio Selection Agents in a CDO

23. An investment bank "structures" a CDO by, among other things, establishing the parameters of the capital structure, such as the debt to equity ratio, the size of each tranche, as well as the interest rate on and price of the notes. An investment bank "underwrites" a CDO by, among other things, purchasing and holding the collateral to be in the portfolio and acting as the initial buyer of protection from the Issuer (the "initial protection buyer"). An investment bank also "places" (*i.e.*, markets and sells) the notes by, among other things, sponsoring the preparation of a private placement memorandum, preparing marketing materials and making presentations and sales pitches to potential purchasers.

24. A "transaction sponsor" proposes that an investment bank underwrite and sell a CDO structured within parameters specified by the transaction sponsor, including,

for example, the nature of the collateral to be included in the underlying portfolio, such as RMBS of a particular rating or year of origination. If the investment bank agrees to structure, underwrite and market the proposed CDO, the transaction sponsor pre-commits to invest in the CDO, customarily by taking a long position in the equity tranche. Because the transaction sponsor invests in the equity -- ensuring that its interests are aligned with other CDO investors -- transaction sponsors customarily play an influential role in the portfolio selection process.

25. A "portfolio selection agent" selects the collateral to be included in the portfolio within the parameters of the CDO established by the investment bank and the transaction sponsor but has no ongoing responsibilities with respect to the collateral once the CDO is launched.

C. The Roles of Goldman Sachs, Paulson and ACA in ABACUS

26. Goldman Sachs was the investment bank that structured ABACUS and placed ABACUS notes on behalf of the Issuer. Goldman Sachs was also the initial protection buyer in ABACUS -- *i.e.*, it purchased protection from the Issuer through a CDS referencing the portfolio.

27. Goldman Sachs expressly misrepresented to ACA that Paulson was to be the transaction sponsor of ABACUS. Acting as the purported transaction sponsor, Paulson specified the parameters of the collateral to be included in the reference portfolio; specified the RMBS to be included in the "initial reference portfolio"; proposed additional RMBS to be included in the final reference portfolio; and vetoed specific RMBS that ACA proposed be included in the final reference portfolio. Paulson paid Goldman Sachs $15 million to structure, underwrite and sell ABACUS.

28. Goldman Sachs misrepresented to ACA that Paulson, as the transaction sponsor, had pre-committed to take a long position in ABACUS -- *i.e.*, that Paulson had an economic incentive to select reference obligations that would perform. In fact, through a separate CDS between Goldman Sachs and Paulson that Goldman Sachs concealed from ACA (the "Goldman Sachs-Paulson CDS"), Paulson purchased from Goldman Sachs the protection on the reference portfolio that Goldman Sachs had purchased from the Issuer as the initial protection buyer, making Paulson the ultimate and undisclosed protection buyer (*i.e.*, the short investor) in ABACUS -- *i.e.*, that Paulson in fact had an economic incentive to select reference obligations that would default. The Goldman Sachs-Paulson CDS was not discoverable through any publicly available source of information.

29. ACA Management, LLC, a wholly owned subsidiary of ACA ("ACAM"), was the *pro forma* portfolio selection agent for ABACUS, *i.e.*, ACAM agreed to and relied upon a portfolio largely selected by Paulson.

30. ACA issued a financial guaranty policy referencing the super senior tranche of ABACUS.

II. Goldman Sachs and Paulson Orchestrated a Massive "RMBS CDO Short" and Fraudulently Induced ACA to Take a Long Position

A. Goldman Sachs Agreed to Structure, Underwrite and Sell ABACUS

31. By 2006, Paulson was convinced that the market for subprime RMBS was on the verge of collapse. Unsatisfied with the enormous profits it already expected to make by shorting individual RMBS and other securities linked to residential mortgages, Paulson sought a way to make a billion dollar profit on the failure of a portfolio of RMBS

through a single transaction. Paulson did not want to take the short position in just any portfolio of RMBS but in a portfolio of RMBS that it had selected and believed was most likely to default.

32. By the fall of 2006, Paulson had identified the characteristics of RMBS that it expected to default in the near future. Paulson then set out to find an investment bank that would structure, underwrite and sell a synthetic CDO with a reference portfolio including RMBS with such characteristics and broker Paulson's purchase of protection on that portfolio.

33. At least one investment bank that Paulson approached before approaching Goldman Sachs declined to assist Paulson out of concern for its reputation. Scott Eichel of Bear Stearns, who reportedly met with Paulson several times, has been quoted as saying that Paulson wanted:

> especially ugly mortgages for the CDOs, like a bettor asking a football owner to bench a star quarterback to improve the odds of his wager against the team.

According to Eichel, such a transaction "didn't pass [Bear's] ethics standards; it was a reputation issue, and it didn't pass our moral compass. We didn't think we should sell deals that someone was shorting on the other side."

34. Likewise, Paulson explored the possibility of being the "sponsor" of a CDO structured by Morgan Stanley, for which Trust Company of the West ("TCW") was the collateral manager. In a February 15, 2007 email, Paulson advised TCW that, "[i]f you do not have a sponsor on the [Morgan Stanley] deal, we would be happy to consider stepping up to bat." As the "sponsor," Paulson would "purchase 100% of the CDO

equity." But, in addition to being the sponsor, Paulson also wanted to "purchase protection on [*i.e.*, short] 100% of the CDO collateral." In an email the next day, TCW replied that Morgan Stanley "may have a tough time with [Paulson] shorting the whole portfolio." Paulson did not, in fact, participate in the Morgan Stanley deal.

35. Paulson also approached Goldman Sachs's Structured Products Correlation Trading Desk, the Goldman Sachs group responsible for underwriting synthetic CDOs referencing portfolios of RMBS (the "Desk"). Like Bear Stearns, Goldman Sachs knew that acting as the investment bank for the transaction that Paulson proposed would entail what Goldman Sachs itself acknowledged was a "reputational risk" -- but that did not stop Goldman Sachs from agreeing to underwrite the transaction on behalf of Paulson, with whom, as the Subcommittee disclosed, Goldman Sachs had done $7 billion in transactions before ABACUS.

36. By February 7, 2007, as reflected in a Goldman Sachs e-mail, Goldman Sachs and Paulson were close to finalizing an engagement letter "for the large RMBS CDO ABACUS trade that will help Paulson short senior tranches of a reference portfolio of Baa2 subprime RMBS risk . . . ." Because ABACUS presented "reputational risk" to Goldman Sachs, Goldman Sachs's Mortgage Capital Committee, which included senior-level management, had to review and approve Goldman Sachs's involvement.

37. A March 12, 2007 memorandum from the Desk to Goldman Sachs's Mortgage Capital Committee plainly identified Paulson and Paulson's economic interest in ABACUS, stating that "Goldman [was] effectively working an order for Paulson to buy protection on [*i.e.*, short] specific layers of the [ABACUS] capital structure." The March 12 memorandum also expressly disclosed the Goldman Sachs-Paulson CDS,

pursuant to which -- unknown to ACA and in direct contradiction of Goldman Sachs's representations to ACA that Paulson was the equity investor in ABACUS -- Paulson purchased from Goldman Sachs the protection on the reference portfolio that Goldman Sachs had purchased from the Issuer, making Paulson the ultimate and undisclosed protection buyer (*i.e.*, the short investor) in ABACUS. Specifically, the March 12 memorandum explained that:

> Goldman's profits come directly from the purchase of credit protection . . . and *simultaneous re-offering of such protection under the same terms for a pre-negotiated premium that will be payable by Paulson.* [emphasis supplied]

38. Nevertheless, to "compete more aggressively in the growing market for synthetics written on structured products," the Mortgage Capital Committee authorized Goldman Sachs to structure, underwrite and sell ABACUS. Goldman Sachs also expected to receive an "upfront premium" from Paulson and projected its profit "to be between $15 million and $20 million."

B. Goldman Sachs And Paulson Learned That Paulson Would Have To "Play The Role Of The Equity Investor" To Find A Portfolio Selection Agent Willing To Participate In ABACUS

39. In the fall of 2006, prior to structuring ABACUS itself, Goldman Sachs structured at least one ABACUS-like super-senior trade to help Paulson short the RMBS market at a macro level. That transaction did not involve a portfolio selection agent. However, Goldman Sachs and Paulson agreed that, in order to consummate another "ABACUS-like" transaction, Goldman Sachs and Paulson would have to engage a portfolio selection agent, which would help market the transaction to potential long investors. Indeed, as set forth in the March 12, 2007 memorandum from the Desk to

Goldman Sachs's Mortgage Capital Committee, Goldman Sachs "expect[ed] to leverage ACA's credibility and franchise to help distribute this Transaction."

40. In December 2006, Goldman Sachs and Paulson set out to identify a portfolio selection agent for ABACUS that would be:

> flexible [with respect to] portfolio selection (i.e. ideally we will send them a list of 200 Baa2-rated 2006-vintage RMBS bonds that fit certain criteria, and the portfolio selection agent will select 100 out of the 200 bonds).

41. As Goldman Sachs and Paulson soon learned, however, they could not find a portfolio selection agent for ABACUS -- much less a financial guaranty insurer to wrap the super senior portion of its capital structure -- if they candidly disclosed that Paulson, the purported "transaction sponsor" proposing the reference portfolio, intended to take an enormous short position against that portfolio.

42. Thus, on January 5, 2007, as disclosed by the Subcommittee, Goldman Sachs and Paulson met with GSC Partners ("GSC"), an institutional investment manager, to ask whether GSC would act as the portfolio selection agent for ABACUS. At the meeting, as reflected in an e-mail made public by the Subcommittee, Goldman Sachs and Paulson expressly disclosed to GSC that Paulson intended to short the reference portfolio of ABACUS. GSC declined to act as the portfolio selection agent because ABACUS posed reputational risk for GSC and the CDO market as whole. Indeed, on February 27, 2007, when Goldman Sachs subsequently began to market ABACUS notes, a senior trader at GSC sent an e-mail to the head of Goldman Sachs's CDO Origination Desk, stating: "I do not have to say how bad it is that you guys are pushing this thing."

43. Moreover, as a representative of Paulson testified in *SEC v. Goldman, Sachs & Co.*, No. 10-CV-3229 (S.D.N.Y. 2010), Paulson knew that it was a "problem in terms of arranging a meeting with a CDO manager" if the manager understood that Paulson was only "interested in shorting securities." Thus:

> in order to get in the room, [Paulson] sometimes took an interest in looking at . . . the equity of a transaction as we were, in fact, equity investors in certain CDOs.

44. For example, at the same time that Paulson was interviewing potential collateral managers for ABACUS, Paulson was also interviewing potential collateral managers for a CDO to be structured by Deutsche Bank. As in ABACUS, Paulson intended to short the CDO. Deutsche Bank arranged for Paulson to interview two collateral managers. In a January 29, 2007 e-mail, Deutsche Bank asked Paulson:

> You're going to *play the role of potential equity investor* when you meet with [the two collateral managers], right? [emphasis supplied]

Paulson confirmed that it would "play the role of [a] potential equity investor," stating:

> I already met with [one of the collateral managers] and I will *stick to the script* with [the other collateral manager]. [emphasis supplied]

45. Thus, Paulson not only knew that it would not be able to retain a portfolio selection agent for ABACUS if it candidly disclosed its true economic interest in ABACUS -- much less a financial guaranty insurer to wrap the super senior portion of its capital structure -- Paulson had a previously-employed and well-rehearsed "script" in which Paulson "played the role" of the "equity investor" in order to mislead others to participate in transactions that Paulson in fact secretly intended to short.

46. By February 7, 2007, as reflected in a Goldman Sachs e-mail, Goldman Sachs and Paulson were close to finalizing an engagement letter "for the large RMBS CDO ABACUS trade that will help Paulson short senior tranches of a reference portfolio of Baa2 subprime RMBS risk . . . ." The draft engagement letter, based on an engagement letter from a prior deal between Goldman Sachs and Paulson, contained a provision prohibiting Paulson from disclosing to any third party, including ACA, that it was the ultimate and undisclosed protection buyer (*i.e.*, the short investor) in ABACUS. Specifically, Section 11 of a February 5, 2007 draft of the engagement letter provided:

> Disclosure of Transaction. Without the prior consent of Goldman, [Paulson] may not discuss or disclose any information about the Offering, any Back-to-Back CDS, any [Paulson] CDS or any transaction relating thereto with any third party other than (i) to its legal, tax, accounting and other professional advisors and (ii) to the extent required by any applicable law.

On a February 8, 2007 draft of the same engagement letter, handwritten notes in the margin next to Section 11 state that the "involvement" of Paulson Credit Opportunities "should be kept confidential."

47. Although Goldman Sachs and Paulson ultimately did not execute the engagement letter, Goldman Sachs and Paulson agreed and understood that ABACUS would be bound by the terms set forth in the draft engagement agreement, including the provision prohibiting Goldman Sachs or Paulson from disclosing Paulson's ultimate and undisclosed short position in ABACUS to ACA or anyone else. As a representative of Paulson testified in *SEC v. Goldman, Sachs & Co.*, No. 10-CV-3229 (S.D.N.Y. 2010), "[t]here was an informal undertaking from the parties that each other's confidentiality would not be violated."

C. Goldman Sachs And Paulson Agreed To Structure And Document ABACUS In A Manner That Concealed Paulson's Short Interest

48. From the outset of the transaction, Paulson was concerned that it would not be able to collect on its short position in ABACUS if Goldman Sachs defaulted on its obligations as the initial protection buyer, as reflected in a January 6, 2007 email from Fabrice Tourre ("Tourre"), a Goldman Sachs employee who had a central role in structuring, underwriting and selling ABACUS:

> Paulson is concerned about counterparty credit risk, even though Paulson has a [credit support agreement] with Goldman -- *Paulson does not have certainty that if Goldman defaults, at that time Paulson would have sufficient collateral from Goldman* . . . .
> [emphasis supplied]

49. Beginning in January 2007, as reflected, for example, in a January 9, 2007 Goldman Sachs email memorializing a meeting with Paulson, Goldman Sachs and Paulson met repeatedly to discuss "how [Paulson] would like to structure the transaction" to address Paulson's concern. Paulson insisted that Goldman Sachs give Paulson the "option to step into [Goldman Sachs's] shoes" as the initial protection buyer. In the January 9, 2007 email, Goldman Sachs summarized Paulson's proposal as follows:

> 1. Goldman, as in our other ABACUS transactions, would be [the] initial swap counterparty under the CDS [with the Issuer] . . . .
>
> 2. Upon [a Goldman Sachs] downgrade to a specified level (assume for now below investment grade), *Goldman would give Paulson the right to cause a transfer [of that CDS] to Paulson.* [emphasis supplied]

50. Goldman Sachs believed that Paulson's right to "step into [Goldman Sachs] shoes" as the initial protection buyer would "need to be disclosed" to other participants in ABACUS, as Goldman Sachs stated in the January 9, 2007 email:

> If so advised by counsel (and I believe they will advise this), *Paulson would be disclosed in the offering documentation as [the] potential replacement counterparty*, and the posting and collateral mechanics described [in the email] *will need to be disclosed.* [emphasis supplied].

51. However, "disclos[ing] [Paulson] in the offering documentation as [the] potential replacement counterparty" would have revealed Paulson's short interest in ABACUS. Instead of doing so, Goldman Sachs and Paulson agreed to document the ABACUS transaction in a manner that concealed Paulson's short interest in ABACUS.

52. Thus, Section 12.7, entitled Replacement of the Credit Default Swap, Basis Swap and Collateral Put Agreement, of the ABACUS Indenture, dated April 26, 2007 (the "Indenture"), gave Goldman Sachs the right to appoint its successor as the initial protection buyer in the event that Goldman Sachs defaulted:

> In an Event of Default or a Termination Event (as such term is defined in the Credit Default Swap, Basis Swap and/or Collateral Put Agreement, as applicable). . . then the Issuer shall automatically terminate the Credit Default Swap . . . and *shall . . . enter into a replacement credit default swap and basis swap with a party nominated by the Protection Buyer* [*i.e.*, Goldman Sachs] . . . . [emphasis supplied].

53. The most straightforward way to accomplish Paulson's objective would have been to draft Section 12.7 of the Indenture to provide that, in an event of default, the Issuer "shall . . . enter into a replacement credit default swap *with [Paulson].*" Instead, to ensure that Paulson would be able to collect on its short position in ABACUS, while at

the same time concealing Paulson's short interest in ABACUS, Goldman Sachs and Paulson entered into a "Side Letter Agreement," also dated April 26, 2007 (the "Side Letter Agreement"), that secretly committed Goldman Sachs to appoint Paulson as its successor as the initial protection buyer in an event of default.

54. Thus, Goldman Sachs and Paulson provided in their Side Letter Agreement that:

> [n]otwithstanding anything to the contrary in the Indenture, we agree that in connection with any replacement of the Credit Default Swap [among other things] pursuant to Section 12.7 of the Indenture, if [Paulson] so requests, [Goldman Sachs] *shall select [Paulson Credit Opportunities] as the Replacement Counterparty* in accordance with Section 12.7 of the Indenture. [emphasis supplied].

Paulson & Co. executed the Side Letter Agreement "as agent for" Paulson Credit Opportunities.

55. The omission of any reference to Paulson in the Indenture -- or anywhere else in the offering materials or transaction documents -- was no accident. To the contrary, Goldman Sachs and Paulson agreed that the Indenture would be drafted to omit any reference to Paulson. For example, in an April 10, 2007 email, Goldman Sachs sent Paulson a draft of the ABACUS Indenture, stating:

> I have attached [Goldman Sachs's] draft Indenture, which will govern the Issuer's ability to enter into replacement transactions. The appropriate section is 12.7, which basically mirrors the disclosure language that [Goldman Sachs] had provided.

The "disclosure language that [Goldman Sachs] had provided" did not disclose Paulson.

56. Although, as Goldman Sachs and Paulson knew, Goldman Sachs provided the misleading Indenture to ACA, neither Goldman Sachs nor Paulson disclosed the Side Letter Agreement to ACA.

D. Goldman Sachs Misrepresented to ACA That Paulson's Economic Interest In The "Capital Structure" Of ABACUS Was "100% Equity"

57. As explained in an internal Goldman Sachs e-mail regarding "ACA/Paulson," it was:

> [Goldman Sachs's] idea to broker the short. Paulson's idea to work with a [portfolio selection agent]. [Goldman Sachs's] idea to discuss this with ACA who could do super senior [wrap] at the same time . . . .

58. On January 8, 2007, Goldman Sachs and Paulson met with ACAM at Paulson's offices in New York City, where they discussed the proposed transaction, including, among other things, the RMBS to be included in the reference portfolio. In contrast to the candid disclosure to GSC and others of Paulson's short interest in ABACUS, neither Goldman Sachs nor Paulson disclosed to ACAM that Paulson intended to short the reference portfolio and had no intention of taking any long position.

59. Goldman Sachs knew that Paulson had not disclosed to ACAM that Paulson intended to short the reference portfolio. In an e-mail regarding the "Paulson meeting" later on January 8, 2007, ACAM expressly asked Goldman Sachs how Paulson intended to "participate" in ABACUS:

> I have no idea how it went – I wouldn't say it went poorly, not at all, but I think it didn't help that we didn't know exactly *how* [*Paulson*] *want*[*s*] *to participate in the space.* Can you get us some feedback? [emphasis supplied]

Although Goldman Sachs responded to ACAM's January 8, 2007 e-mail, it did not tell ACAM the truth -- that Paulson intended to "participate" in ABACUS by shorting the reference portfolio.

60. Instead, in a January 10, 2007 e-mail to ACA purporting to provide a "Transaction Summary," Goldman Sachs affirmatively and fraudulently misrepresented that Paulson and ACAM shared a common economic interest in ABACUS by representing that the "compensation structure *aligns everyone's incentives*: the Transaction Sponsor [*i.e.*, Paulson], the Portfolio Selection Agent [*i.e.*, ACAM] and Goldman." (emphasis supplied). In fact, as Goldman Sachs knew, the economic interests of Paulson and ACAM in ABACUS were in direct and irreconcilable conflict. Indeed, as a representative of Paulson itself has since testified, Paulson's and ACAM's economic incentives in selecting the reference obligations for ABACUS were "exactly opposite."

61. As a former managing director of Moody's Investors Services, Inc., the rating agency that rated ABACUS notes, testified before the Subcommittee, Paulson's short position in ABACUS was a stark departure from the "basic assumption" in the financial industry that the people "putting deals together [] want the deal to succeed." As set forth in the Subcommittee's final report, entitled "Wall Street and the Financial Crisis: Anatomy of a Financial Collapse," the Moody's representative testified that Paulson's short interest in ABACUS and its involvement in selecting the reference portfolio *"change[d] the incentives in the structure"*:

> [I]t is something that [Moody's] would have wanted to know because it is more of a qualitative not a quantitative assessment if someone who intends the deal to blow up is

> picking the portfolio . . . . It just changes the whole dynamic of the structure where the person who is putting it together, choosing it, wants it to blow up.

62. Not only did Goldman Sachs misrepresent that Paulson's and ACA's economic interest in ABACUS were "aligned," Goldman Sachs further misrepresented that Paulson was the equity investor in ABACUS, *i.e.*, that among all of the investors taking a long position in ABACUS, Paulson had the greatest risk of loss. Thus, also in its January 10, 2007 e-mail to ACA, Goldman Sachs identified Paulson as the "Transaction Sponsor," described the "Contemplated Capital Structure" of ABACUS by tranche, and indicated that the lowest tranche, "[0]%-[9]%" -- *i.e.*, the equity tranche -- was "pre-committed first loss." In plain language, as a Goldman Sachs employee who participated in structuring ABACUS testified, Goldman Sachs's January 10, 2007 e-mail communicated to ACA that Paulson was "keeping" the equity tranche in ABACUS:

> Q. At this point had an investor been identified for the zero to nine percent risk?
>
> A. I mean, as I mentioned, we weren't looking to like actually go out and distribute that risk. So -- I think *the way I read this is just that it's essentially that, you know, essentially, Paulson is keeping that risk.* [emphasis supplied]

In fact, as Goldman Sachs knew, and contrary to its misrepresentations to ACA, Paulson never intended, let alone committed, to take an equity position in ABACUS but instead always intended to short the ABACUS portfolio.

63. Goldman Sachs knew that it had successfully misled ACAM into believing that Paulson had pre-committed to take a long position in ABACUS. On January 14, 2007, the Chief Operating Officer of ACAM sent an e-mail to a Goldman

Sachs Managing Director, in which ACAM specifically referred to Paulson's "equity perspective" in ABACUS. The email was forwarded internally to others at Goldman Sachs, including to Tourre. Although Goldman Sachs replied to ACAM's e-mail, Goldman Sachs did not correct ACAM's manifest misunderstanding that Paulson was to invest in the equity of ABACUS. By undertaking to characterize Paulson's economic interest in the transaction, Goldman Sachs assumed a duty to disclose Paulson's true economic interest in ABACUS, especially once it was put on notice that ACA was acting on the erroneous belief, based on, among other things, Goldman Sachs's affirmative misrepresentations, that Paulson had pre-committed to take a long position in ABACUS.

64. In a telephone conversation on January 17, 2007, a Goldman Sachs Managing Director expressly and unequivocally misrepresented to ACAM that Paulson's economic interest in the "capital structure" of ABACUS was "100% equity." An audio recording of the January 17 call includes the following exchanges:

ACAM:	Okay. What were you [and another ACAM employee] talking about?
Goldman Sachs:	We're working on something potentially that could happen. We're not there yet, but we're getting close.
ACAM:	Uh huh.
Goldman Sachs:	Um, where you would be managing a pool where we're placing a hundred percent of the equity.
	...
ACAM:	Is it uh, confidential who [the investor] is at this point?
Goldman Sachs:	Um, I think so. [The other ACAM employee] knows, but I'm not sure how she is handling it.
ACAM:	[Laughing] Oh, okay. Oh, all right. No, I'm

Goldman Sachs: Do you want me to tell you? I'll tell you. I'm happy to tell you.

ACAM: Yeah! Sure.

Goldman Sachs: Okay. Don't say I said anything.

ACAM: Yeah.

Goldman Sachs: Paulson.

ACAM: Mmm.

Goldman Sachs: Do you know them?

ACAM: No.

Goldman Sachs: They are a multi-strategy fund. Very, very large, that does not focus on the credit part of the curve, typically. They are more in high yield, um, you know, corporate stuff. Things that are away from mortgages. So this is their first foray into it. And they'd manage around that equity potentially by doing other things within ABS, but they're just first getting started here

ACAM: Uh huh.

Goldman Sachs: Um, we have a long-standing relationship with them so they're only just testing this with us and they only asked to meet three people.

ACAM: Hmm. And so they, we'd be looking at, what part of the capital structure?

Goldman Sachs: All, 100% equity.

...

ACAM: to [The previously-referenced ACAM employee is] the right person talk to, you know.

Goldman Sachs: Right, so were just going, you know, it's just a matter of all that stuff, cause then it gets into a legal issue and all that other stuff and so, you know, no point in involving you guys in the portfolio selection, but my guess is [the previously-referenced ACAM employee is] going to be coming to you guys for portfolio selection next.

ACAM: Right. Well, no problem.

Goldman Sachs: Being totally honest, right.

65. On February 12, 2007, ACA's Commitments Committee met to formally consider ACAM's participation in ABACUS as portfolio selection agent. The memorandum submitted by the ACAM employees communicating with Goldman Sachs concerning ABACUS to the Commitments Committee memorializes ACAM's belief, based on Goldman Sachs's misrepresentations and omissions, that Paulson was the:

> *equity investor* [that] wanted to invest in the 0-9% tranche of a static mezzanine ABS CDO backed 100% by subprime residential mortgage securities. [emphasis supplied]

At the meeting, as reflected in contemporaneous handwritten notes of a member of the Commitments Committee present at the meeting, the Commitments Committee specifically discussed ACAM's "portfolio selection work with the equity investor."

66. On February 23, 2007, Goldman Sachs repeated and confirmed its misrepresentation that Paulson had agreed to be the equity investor in ABACUS. Contemporaneous notes memorializing a telephone conversation between ACA and Goldman Sachs state:

> 2/23 Call w/ [Goldman Sachs] -- *Counterparty motivation* -- reverse inquiry from Paulson who interviewed several collateral management teams -- one being ACA. *Paulson looking 0-10%.* [emphasis supplied].

By "reverse inquiry," Goldman Sachs meant that Paulson had approached Goldman Sachs to propose that it structure and market ABACUS.

67. A February 27, 2007 internal memorandum to ACA's Senior Credit Committee -- the committee responsible for authorizing ACA to issue financial guaranty policies, including the super senior wrap of ABACUS -- includes a sub-section entitled "Transaction Motivation," which states, based on Goldman Sachs's misrepresentations and omissions: "this transaction was sourced as a reverse inquiry *from the equity investor*." (emphasis supplied).

68. In sum, Goldman Sachs misrepresented that Paulson had pre-committed to take "100% equity" in the "capital structure" of ABACUS, and Goldman Sachs and Paulson concealed that Paulson was in fact the sole short investor in ABACUS. As alleged below, reasonably relying on these misrepresentations and omissions, ACA entered into a financial guaranty policy referencing the super senior tranche of ABACUS and was injured as a direct and proximate result.

E. Paulson Participated in Selecting the Reference Portfolio to Ensure that it Would Fail

69. Paulson used its role as the purported transaction sponsor to manipulate the portfolio selection process to the detriment of every long position in ABACUS. In or about January 2007, Paulson initiated the portfolio selection process by providing Goldman Sachs with its selection criteria. Goldman Sachs then provided Paulson with a spreadsheet of RMBS meeting Paulson's criteria, from which Paulson selected 123 RMBS.

70. On January 9, 2007, Goldman Sachs sent ACAM an e-mail regarding the "Paulson Portfolio" attaching a list of 123 RMBS to be considered for inclusion in the reference portfolio.

71. On January 22, 2007, ACAM sent an e-mail to Goldman Sachs regarding the "Paulson Portfolio," identifying "86 subprime mortgage positions that [ACAM] would recommend taking exposure to synthetically," including 55 of those "originally submitted to [ACAM] for review."

72. On February 2, 2007, Goldman Sachs, Paulson and ACAM representatives met at ACA's offices to discuss the RMBS to be included in the reference portfolio. While sitting in the meeting, Tourre sent an e-mail to a Goldman Sachs colleague, stating, "I am at this ACA Paulson meeting, this is surreal." What he meant by "surreal" was that, at the meeting, Paulson proposed RMBS, ostensibly in a good faith effort to select those that it considered *least* likely to default, when in fact -- as Goldman Sachs was acutely aware and ACAM did not know -- Paulson proposed RMBS that it considered *most* likely to default.

73. Shortly after the meeting, Paulson e-mailed ACAM, copying Goldman Sachs, to explain the purported reasons for Paulson's proposed changes to the reference portfolio, falsely representing that its changes were intended to have a "neutral overall result":

> I apologize for not explaining more clearly that [Paulson] had taken the whole portfolio to the Baa2 level, migrated both A3 and Baa3 to Baa2, assuming that the migration in opposite directions would have a *neutral overall result.* (Emphasis supplied.)

74. In fact, far from intending a "neutral overall result," as a representative of Paulson itself has testified, Paulson's proposed changes to the reference portfolio were designed to include as many RMBS as possible that Paulson believed "weren't going to perform":

Q: [Paulson's] portfolio analysis was designed in large part to identify bonds that weren't going to perform, right?

A: Right.

Q: Because [Paulson] wanted to short those bonds?

A: Right.

Q: And as far as [Paulson was] aware, the focus of ACA's analysis of the portfolio was different, right?

A: Exactly.

Q: In fact, [ACA's] aim was in many ways opposite yours?

A: It was exactly opposite ours.

Q: They were trying to identify bonds that in their view were going to perform.

A: Exactly.

75. Later on February 2, 2007, ACAM e-mailed Paulson and Goldman Sachs a list of 100 RMBS to be included in the reference portfolio, including 79 RMBS on which ACAM and Paulson "concur[ed] as well as 21 replacement" RMBS proposed by ACAM.

76. By e-mail dated February 5, 2007, Paulson circulated a "revised portfolio" of 92 RMBS to ACAM and Goldman Sachs. Reinforcing the false impression that Paulson shared ACAM's economic interest in a strong quality reference portfolio, Paulson explained:

> I attach the portfolio you proposed with eight deletions. Two are duplicates and the others are either too seasoned or have some other characteristics that make them *too risky from Paulson's perspective*. [emphasis supplied]

As Goldman Sachs knew, because ACAM had told Goldman Sachs in a January 14, 2007 e-mail, ACAM understood that Paulson's "perspective" was the "equity perspective." Nevertheless, Goldman Sachs remained silent.

77. Further reinforcing ACA's false understanding that Paulson shared ACAM's economic interest in a strong quality reference portfolio, Paulson also stated in its February 5, 2007 e-mail that, according to Goldman Sachs, Paulson's "revised portfolio" provided "sufficient diversification." As Goldman Sachs and Paulson both knew, "diversification" is a well-recognized means of reducing risk.

78. By e-mail dated February 6, 2007, Paulson circulated a "final portfolio" of 90 RMBS to ACAM and Goldman Sachs. The final portfolio contained 49 RMBS originally proposed by Paulson -- more than enough to ensure that Paulson (as the ultimate and undisclosed protection buyer) would receive enormous contingent payments under any financial guaranty policy referencing the super senior tranche of ABACUS.

79. Goldman Sachs knew that Paulson had played an instrumental role in the portfolio selection process. For example, a long investor that ultimately purchased ABACUS notes asked Goldman Sachs if certain bonds could be removed from the ABACUS portfolio. On March 12, 2007, in an internal Goldman Sachs e-mail, Tourre rejected that request on the ground that Paulson -- not ACAM -- "will likely not agree to this unless we tell [Paulson] that nobody will buy [ABACUS notes] if we don't make that change."

80. Paulson knew that ACAM mistakenly believed Paulson to be a long investor in ABACUS. On April 9, 2007, the Chief Operating Officer of ACAM sent an e-mail to a Paulson representative, reflecting ACAM's understanding that Paulson was

going to "invest" in ABACUS. ACAM advised Paulson, "we are going to *invest as well*, approximately $40 million in Class A2 for some of our funds" (emphasis supplied) for Zenith Funding, Ltd., Grenadier Funding, Ltd., and ACA ABS 2003-2, Ltd. Thus, ACAM advised Paulson that, in its capacity as the collateral manager for certain funds, ACAM intended to direct those funds to "invest" in ABACUS -- *i.e.*, take a long position in ABACUS -- which ACAM understood Paulson was going to do "as well." Paulson did not correct ACAM's manifest misunderstanding that Paulson was going take a long position in ABACUS.

F. ACA "Wrapped" the Super Senior Tranche of ABACUS

81. On January 27, 2007, Paulson approached ACA "to talk about the super senior" wrap in ABACUS. Because ACA understood, based on Goldman Sachs's and Paulson's misrepresentations and omissions, that Paulson was a long investor in ABACUS -- and therefore had an economic incentive to pick reference obligations that would perform -- ACA agreed to consider issuing a financial guaranty policy referencing the super senior tranche of ABACUS.

82. On March 30, 2007, ACA's Senior Credit Committee met to review ACA's proposed sale of "protection on [the] 50-100% tranche" of ABACUS (*i.e.*, the "super senior" tranche) for 50 basis points per year.

83. ACA's Senior Credit Committee reviewed and relied on, among other things, the February 12, 2007 memorandum to ACAM's Commitments Committee and the February 27, 2007 memorandum to the Senior Credit Committee, each of which -- based on Goldman Sachs's and Paulson's misrepresentations and omissions -- expressly stated that Paulson was the "equity investor" in ABACUS.

84. Reasonably relying on Goldman Sachs's false representation that Paulson had pre-committed to take a long position in ABACUS -- and thus supposedly shared a common economic interest with ACA in selecting reference obligations that would perform -- the Senior Credit Committee authorized ACA to issue a financial guaranty policy on the super senior tranche of ABACUS.

85. In the period between the Senior Credit Committee's conditional approval of the financial guaranty policy on March 31, 2007 and the consummation of that policy on May 31, 2007, ACA continued to believe that Paulson had taken a long position in ABACUS.

86. For example, in an April 10, 2007 email, the Chief Operating Officer of ACAM informed the ACAM "CDO Team" that Goldman Sachs had "priced [*i.e.*, obtained commitments to buy] $192 million of Class A1 and A2 [notes]" in ABACUS and stated that:

> the transaction came about as a reverse inquiry, a big hedge fund new to ACA chose us out of 3 managers they met with and *they [i.e., Paulson] are investing in the 0-10% tranche (equity through BBB).* Goldman still hopes to attract additional investors and price additional [notes] over the next few weeks (this is not a fully distributed transaction). [emphasis supplied]

87. Similarly, in a separate April 10, 2007 email, the Chief Operating Officer of ACAM informed the Chief Operating Officer of ACA and other senior executives that Goldman Sachs had:

> priced $192 million in total of Class A1 and A2 [notes] today to settle on April 26. *Paulson took down a proportionate amount of equity (0-10% tranche).* [emphasis supplied].

88. Likewise, a May 17, 2007 e-mail from the Chief Operating Officer of ACAM to members of the Senior Credit Committee states that Paulson intended to "sell protection on [] the 0-10% tranche," *i.e.*, take a long position in the equity tranche of ABACUS through a CDS.

89. At the insistence of Goldman Sachs, ABN AMRO Bank N.V. ("ABN") "intermediated" ACA's financial guaranty policy. Thus, ABN issued to Goldman Sachs a financial guaranty policy referencing the super senior tranche of ABACUS. ACA in turn issued to ABN a financial guaranty policy referencing the super senior tranche of ABACUS. In effect, ABN assumed the risk that ACA would default on its financial guaranty policy, while Goldman Sachs insulated itself from the risk that ACA would default on its financial guaranty policy.

90. On or about May 31, 2007, ACA issued to ABN a financial guaranty policy referencing the super senior tranche of ABACUS for up to $909 million for an annual premium of $4.5 million, pursuant to: (i) the Credit Default Swap Insurance Policy, effective May 31, 2007; (ii) the 1992 ISDA Master Agreement, dated as of May 31, 2007, between ABN and ACA Credit Products - ABN AMRO, LLC; (iii) the Schedule to the Master Agreement, dated as of May 31, 2007; and (iv) the Confirmation of Credit Default Swap Transaction, between ABN and ACA Credit Products, dated May 31, 2007.

91. Had ACA known that Paulson, which played an influential role in selecting the reference portfolio, did not have any long position in ABACUS but instead was the sole short investor, ACA would not have agreed to enter into a financial guaranty policy referencing the super senior tranche of ABACUS. Among other things, knowledge of Paulson's true economic interests would have raised a red flag and caused senior ACA personnel to decline to approve any participation in the transaction. In short, as ACA's Chief Risk Officer at the time has since stated: "We were misled and led into a deal we otherwise would not have done."

G. Goldman Sachs Failed To Unload All Risk In ABACUS

92. By the "early summer of 2006," Goldman Sachs, like Paulson, was convinced that the market for subprime RMBS was "going to have a very unhappy ending." Thus, as the Managing Director of Goldman Sachs's mortgage trading desk stated in his 2007 annual performance evaluation, he directed Goldman Sachs's mortgage trading desk to "enter into efficient shorts in both the RMBS and CDO space." As Goldman Sachs's Chief Risk Officer also later explained in an October 29, 2007 "Tax Department Presentation":

> Starting early in '07 [Goldman Sachs's] mortgage trading desk *started putting on big short positions* . . . and did so in enough quantity that *we were net short*, and made money (substantial $$ in the 3rd quarter [of 2007]) as the subprime market weakened. [emphasis supplied]

Indeed, by 2007, as disclosed by the Subcommittee, Goldman Sachs had a $13.9 billion net short position in subprime RMBS.

93. Notwithstanding Goldman Sachs's belief that the market for subprime RMBS was on the verge of collapse -- as evidenced by its $13.9 billion net short position -- Goldman Sachs agreed to structure ABACUS and sell its short position as the initial protection buyer to Paulson because, as a market maker, Goldman Sachs was in the business of structuring transactions for others for profit.

94. As stated in an October 27, 2006 Goldman Sachs email, when Paulson first expressed its "appetite to short . . . a Baa2 2006 vintage RMBS portfolio," the Managing Director of Goldman Sachs's mortgage trading desk queried, "Honestly why are we not doing this for ourselves?", to which a Goldman Sachs colleague replied:

> [Paulson] will do it away from us if we don't do it. *We already are working on doing this for ourselves* [in other deals]. [emphasis supplied].

In other words, Goldman Sachs had ample alternative opportunities to satisfy its own "appetite to short" subprime RMBS and, if Goldman Sachs had declined to help Paulson do the same, Paulson would take its lucrative business elsewhere.

95. As Tourre further explained in a January 16, 2007 email, structuring ABACUS to help Paulson accomplish a macro short on the subprime RMBS market was advantageous to Goldman Sachs because

> (a) this is easy business, (b) with little risk for Goldman Sachs, (c) business that we can do in size, (d) that we are not axed on as principal and (e) where we can charge approx[imately] 25 [basis points] on the trade notional (between $1bn and $2bn).

96. As originally conceived, Goldman Sachs had no intention of taking any risk, long or short, in ABACUS. As Tourre explained in a February 7, 2007 email to his colleagues at Goldman Sachs:

> At the time we distribute, [Goldman Sachs] will cross the tranches into Paulson [*i.e.*, sell its short position as the initial protection buyer to Paulson] -- therefore no commitment for [Goldman Sachs] to take down any risk.

97. However, in early May 2007, a few weeks before ABACUS closed, Paulson advised Goldman Sachs that Paulson wanted to short 5% more of the capital structure of ABACUS than ACA had agreed to wrap. As Tourre stated in a May 8, 2007 email, Paulson's new position presented Goldman Sachs with two options. "Option 1:" Goldman Sachs could decline to sell Paulson any protection on the ABACUS portfolio beyond ACA's wrap, in which case Goldman Sachs "would make risk-free approx[imately] $14 [million]." "Option 2": Goldman Sachs could agree to sell Paulson 5% more protection on the ABACUS portfolio that ACA had agreed to wrap, in which case:

> [Goldman Sachs] would be at risk on $100 [million] of the [additional 5%] tranche, but assuming we can trade that tranche at approx[imately] 100 [basis points] spread (which I am confident we can do), *[Goldman Sachs] would make $18 [million]*. [emphasis supplied]

98. To accommodate an important client and create the opportunity to increase Goldman Sachs's profit in ABACUS from $14 to $18 million, Goldman Sachs chose "Option 2." As Tourre explained shortly after ABACUS closed, in a June 4, 2007 email chain, ABACUS was:

> a good trade for [Goldman Sachs] from a [profit and loss] standpoint. On[c]e we completely finish up this Paulson/ABACUS 07-AC1 trade, we will have made over $15 [million] pretty much risk free. . . . . *We have some money left to make in the open risk positions we have, as well as future business we can do with Paulson . . .* [emphasis supplied]

99. Goldman Sachs's agreement to take a long position in 5% of the capital structure of ABACUS in no way suggests that Goldman Sachs did not know that Paulson had used its role as the purported transaction sponsor to manipulate the portfolio selection process to the detriment of every long position in ABACUS. To the contrary, Goldman Sachs was fully aware that Paulson had selected reference obligations that it believed would default. Goldman Sachs only agreed to take a small long position in ABACUS because it was "confident" that it could quickly sell that position to investors for a substantial profit. In any event, as Goldman Sachs's Chief Operating Officer testified before the Financial Crisis Inquiry Commission, Goldman Sachs "looks at [its] risk in the aggregate." Thus, any long risk in ABACUS that Goldman Sachs agreed to take on a temporary basis was offset by Goldman Sachs's $13.9 billion net short position in subprime RMBS.

100. Tourre testified at the April 27, 2010 Subcommittee Hearing as follows:

> **Senator Levin**: Did Goldman intend to keep a long stake in that transaction when the deal was structured? I know it ended up with a piece. Was it intended that it end up with a piece of that deal?
>
> **Mr. Tourre**: We tried to hedge our risk by selling that piece as well, but were not successful in doing so.
>
> **Senator Levin**: So it was intended to sell that piece?
>
> **Mr. Tourre**: For prudent risk management reasons, we were trying—

> **Senator Levin**: Oh, I am sure for all the right reasons. But it was intended that Goldman not have any long stake on that piece. Is that correct?
>
> **Mr. Tourre**: Yes.

III. Goldman Sachs Aggressively Peddled Synthetic RMBS CDOs With Total Indifference to Their Impact on Investors and The Financial Markets

101. In late 2004, Goldman Sachs established the Structured Products Correlation Trading Desk at its headquarters in New York City. The Desk acted as the underwriter for a series of synthetic CDOs referencing portfolios of RMBS, including ABACUS.

102. Goldman Sachs aggressively protected and expanded the Desk's profitable "franchise" for synthetic CDOs. An internal memorandum dated March 12, 2007 addressed to Goldman Sachs's Mortgage Capital Committee, stated that the "ability to structure and execute complicated transactions to meet multiple client's needs and objectives is key for our franchise," and "[e]xecuting this transaction [ABACUS] and others like it helps position [Goldman Sachs] to compete more aggressively in the growing market for synthetics written on structured products," which was a huge and enormously profitable market for Goldman Sachs. As disclosed in the Financial Crisis Inquiry Report, between July 1, 2004 and May 31, 2007, Goldman Sachs structured 47 synthetic CDOs with an aggregate face value of $66 billion -- all of which generated underwriting fees and other profits for Goldman Sachs.

103. On April 27, 2010, the Subcommittee held a hearing "on the role of investment banks in the [United States financial] crisis, using Goldman Sachs as a case study." The Subcommittee made the "following findings of fact," among others:

> (2) **Magnifying risk.** Goldman Sachs magnified the impact of toxic mortgages on financial markets by re-securitizing RMBS securities in [CDOs], referencing them in synthetic CDOs, selling the CDO securities to investors . . . .
>
> (5) **Abacus Transaction.** Goldman Sachs . . . did not disclose to the Moody's analyst overseeing the rating of the CDO that a hedge fund client taking a short position in the CDO had helped to select the referenced assets, *and also did not disclose that fact to other investors*. [emphasis supplied]

104. Citing ABACUS as a prominent example, the Subcommittee concluded that Goldman Sachs was one of the "self-interested promoters of risky and complicated financial schemes that helped trigger the [financial] crisis."

105. The Subcommittee's final report, entitled "Wall Street and the Financial Crisis: Anatomy of a Financial Collapse," concluded that Goldman Sachs had:

> allowed a hedge fund, Paulson & Co. Inc., that planned on shorting the CDO, to play a major but hidden role in selecting its assets. Goldman marketed Abacus securities to its clients, knowing the CDO was designed to lose value and without disclosing the hedge fund's asset selection role or investment objective to potential investors. Three long investors [including ACA] together lost about $1 billion from their Abacus investments, while the Paulson hedge fund profited by about the same amount. Today, the Abacus securities are worthless.

106. Goldman Sachs's total disregard for the damage inflicted on the participants in its synthetic RMBS CDOs -- and the United States financial markets themselves -- was starkly illustrated by the contemporaneous e-mails of Fabrice Tourre.

As a Vice President on the Desk, Tourre had a central role in structuring, underwriting and selling ABACUS. Goldman Sachs has since promoted Tourre to Executive Director of Goldman Sachs International in London.

107. On January 23, 2007, Tourre e-mailed a Goldman Sachs colleague (in English translation where applicable):

> More and more leverage in the system, The whole building is about to collapse anytime now. Only potential survivor, the fabulous Fab[rice Tourre]... standing in the middle of all these complex, highly leveraged, exotic trades he created without necessarily understanding all of the implications of those monstrosities!!!

108. On January 29, 2007, Tourre e-mailed a Goldman Sachs colleague (in English translation where applicable):

> When I think that I had some input into the creation of this product . . . which you invent telling yourself: "Well, what if we created a "thing", which has no purpose, which is absolutely conceptual and highly theoretical and which nobody knows how to price?") it sickens the heart to see it shot down in mid-flight...It's a little like Frankenstein turning against his own inventor :).

109. On March 7, 2007, Tourre e-mailed a Goldman Sachs colleague that Daniel Sparks, the former head of Goldman Sachs's mortgage department, believed "that business is totally dead, and the poor little subprime borrowers will not last so long!!!"

110. On June 13, 2007, Tourre e-mailed a Goldman Sachs colleague, stating: "By the way, I have just sold a few Abacus bonds to some widows and orphans that I met at the airport." (English translation).

IV. ACA Was Damaged By Goldman Sachs's and Paulson's Misconduct

111. On or about August 7, 2008, ABN unwound the financial guaranty policy it had issued to Goldman Sachs referencing the super senior tranche of ABACUS, paying Goldman Sachs $840,909,090.

112. Pursuant to the Goldman Sachs-Paulson CDS -- the CDS that Goldman Sachs and Paulson had concealed from ACA -- most of the $840,909,090 paid by ABN to Goldman Sachs was in turn paid by Goldman Sachs to Paulson.

113. By that time, ACA was in severe economic distress and unable to pay its obligations under the financial guaranty policy it had issued to ABN. On August 8, 2008, ACA and counterparties to its structured finance products reached an agreement on a restructuring plan for ACA. The plan provided for the settlement of ACA's structured finance obligations, including those between ACA and ABN. To settle its obligations to ABN under the financial guaranty policy referencing the super senior tranche of ABACUS, ACA paid ABN approximately $15 million in cash and gave ABN surplus notes worth at least $15 million.

114. Had ACA known that Paulson, which played an influential role in selecting the reference portfolio, did not plan to and, in fact, did not take any equity position but instead was the short investor in ABACUS, ACA would not have issued a financial guaranty policy referencing the super senior tranche of ABACUS to ABN.

115. Accordingly, Goldman Sachs and Paulson's misrepresentations and concealments were the direct and proximate cause of ACA's losses pursuant to ACA's financial guaranty policy with ABN.

FIRST CAUSE OF ACTION
(Fraudulent Inducement – Against Goldman Sachs)

116. ACA repeats and re-alleges paragraphs 1 through _ hereof as though fully set forth herein.

117. Goldman Sachs knowingly or recklessly misrepresented to and concealed from ACA material facts with the intent to deceive ACA into believing that Paulson had taken a long position in ABACUS and to conceal Paulson's short position in ABACUS.

118. Goldman Sachs intended its misrepresentations and omissions to induce ACA to guaranty the super senior tranche of ABACUS's capital structure.

119. ACA reasonably relied on Goldman Sachs's misrepresentations and omissions in deciding to wrap the super senior tranche of ABACUS's capital structure.

120. As set forth above, Goldman Sachs engaged in intentional, willful and malicious misconduct in utter disregard for the severe adverse economic consequences for ACA and other participants in ABACUS, as well as the United States financial markets, evincing a high degree of moral turpitude and wanton dishonesty.

121. As a direct and proximate result of Goldman Sachs's misrepresentations and omissions, ACA has been damaged and is entitled to recover compensatory damages in an amount to be determined at trial of at least $30 million, as well as punitive damages in an amount to be determined at trial of at least $90 million.

SECOND CAUSE OF ACTION
(Fraudulent Concealment -- Against Goldman Sachs)

122. ACA repeats and re-alleges paragraphs 1 through _ hereof as though fully set forth herein.

123. Goldman Sachs knew and intentionally failed to disclose to ACA that Paulson had a short position in ABACUS, with the intent that ACA rely and act upon a false belief that Paulson had a long position in ABACUS.

124. Goldman Sachs had a duty to disclose to ACA that Paulson had a short economic interest in ABACUS for the following reasons, among others: (i) Goldman Sachs had superior knowledge of Paulson's economic interest in ABACUS, which ACA was unable to discern through reasonable intelligence or due diligence; (ii) by undertaking to characterize Paulson's economic interest in the ABACUS, Goldman Sachs assumed a duty to disclose Paulson's true economic interest in ABACUS; and (iii) Goldman Sachs was on notice that ACA was acting on the erroneous belief, based on Goldman Sachs's misrepresentations, that Paulson had a long economic interest in ABACUS.

125. ACA reasonably relied on Goldman Sachs's misrepresentations and omissions in deciding to wrap the super senior tranche of ABACUS's capital structure.

126. As set forth above, Goldman Sachs engaged in intentional, willful and malicious misconduct in utter disregard for the severe adverse economic consequences for ACA and other participants in ABACUS, as well as the United States financial markets, evincing a high degree of moral turpitude and wanton dishonesty.

127. As a direct and proximate result of Goldman Sachs's misrepresentations and omissions, ACA has been damaged and is entitled to recover compensatory damages in an amount to be determined at trial of at least $30 million, as well as punitive damages in an amount to be determined at trial of at least $90 million.

THIRD CAUSE OF ACTION
(Fraudulent Inducement – Against Paulson)

128. ACA repeats and re-alleges paragraphs 1 through _ hereof as though fully set forth herein.

129. As part of a common scheme and conspiracy to fraudulently induce ACA to wrap the super senior tranche of ABACUS's capital structure by deceiving ACA into believing that Paulson was to be the equity investor in ABACUS, Paulson and Goldman Sachs agreed, among other things, that Goldman Sachs and Paulson would structure the transaction in a manner -- through what Paulson and Goldman Sachs called their "Side Letter Agreement" -- that concealed Paulson's short interest in ABACUS.

130. Paulson and Goldman Sachs committed overt acts in furtherance of their common scheme and conspiracy to fraudulently induce ACA to wrap the super senior tranche of ABACUS's capital structure. For example, among other things, Goldman Sachs sent a January 10, 2007 e-mail to ACA purporting to provide a "Transaction Summary," in which Goldman Sachs fraudulently misrepresented to ACA that Paulson was (i) the "Transaction Sponsor," (ii) had "pre-committed" to invest in the equity of ABACUS, and (iii) shared a common economic interest in ABACUS with long investors.

131. Paulson and Goldman Sachs knowingly and intentionally participated in their common scheme and conspiracy to fraudulently induce ACA to wrap the super senior tranche of ABACUS's capital structure. For example, to ensure that Paulson would be able to collect on its short position in ABACUS even if Goldman Sachs defaulted, while at the same time continuing to conceal Paulson's true economic interest in ABACUS, Goldman Sachs and Paulson entered into a "Side Letter Agreement" that

secretly committed Goldman Sachs to appoint Paulson as its successor as the initial protection buyer.

132. By reason of the foregoing, ACA has been damaged and is entitled to recover from Paulson, jointly and severally with Goldman Sachs, compensatory damages in an amount to be determined at trial of at least $30 million, as well as punitive damages in an amount to be determined at trial of at least $90 million.

FOURTH CAUSE OF ACTION
(Fraudulent Concealment – Against Paulson)

133. ACA repeats and re-alleges paragraphs 1 through _ hereof as though fully set forth herein.

134. Paulson knew and intentionally failed to disclose to ACA that Paulson had a short position in ABACUS, with the intent that ACA rely and act upon a false belief that Paulson had a long position in ABACUS.

135. Paulson had a duty to disclose to ACA that it had a short economic interest in ABACUS for the following reasons, among others: (i) Paulson had superior knowledge of its economic interest in ABACUS, which ACA was unable to discern through reasonable intelligence or due diligence; (ii) by undertaking to characterize its economic interest in ABACUS, Paulson assumed a duty to disclose Paulson's true economic interest in ABACUS; and (iii) Paulson was on notice that ACA was acting on the erroneous belief that Paulson had a long economic interest in ABACUS.

136. ACA reasonably relied on Paulson's misrepresentations and omissions in deciding to wrap the super senior tranche of ABACUS's capital structure.

137. As set forth above, Paulson engaged in intentional, willful and malicious misconduct in utter disregard for the severe adverse economic consequences for ACA and other participants in ABACUS, as well as the United States financial markets, evincing a high degree of moral turpitude and wanton dishonesty.

138. As a direct and proximate result of Paulson's misrepresentations and omissions, ACA has been damaged and is entitled to recover compensatory damages in an amount to be determined at trial of at least $30 million, as well as punitive damages in an amount to be determined at trial of at least $90 million.

FIFTH CAUSE OF ACTION
(Aiding and Abetting Fraud -- Against Paulson)

139. ACA repeats and re-alleges paragraphs 1 through _ hereof as though fully set forth herein.

140. Paulson had actual knowledge of Goldman Sachs' scheme to fraudulently induce ACA to wrap the super senior tranche of ABACUS's capital structure by deceiving ACA into believing that Paulson was to be the equity investor in ABACUS.

141. Paulson provided Goldman Sachs substantial assistance in achieving Goldman Sachs' fraudulent scheme by: (i) assisting Goldman Sachs to perpetrate the fraudulent scheme by "play[ing] the role" of the "equity investor" in ABACUS; (ii) helping Goldman Sachs conceal the fraudulent scheme by agreeing to conceal from ACA Paulson's short position in ABACUS, and (iii) concealing from ACA Paulson's short position in ABACUS when put on notice that ACA mistakenly believed that Paulson had a long position in ABACUS.

142. As a direct and proximate result of Paulson's unlawful conduct, ACA was damaged and is entitled to recover compensatory damages in an amount to be determined at trial of at least $30 million, as well as punitive damages in an amount to be determined at trial of at least $90 million.

SIXTH CAUSE OF ACTION
(Unjust Enrichment – Against Paulson)

143. ACA repeats and re-alleges paragraphs 1 through _ hereof as though fully set forth herein.

144. Paulson was unjustly enriched at ACA's expense as a result of its misconduct set forth above.

145. As set forth above, the circumstances are such that equity and good conscience require Paulson to return to ACA all of the money that it obtained at ACA's expense in an amount to be determined at trial.

WHEREFORE, ACA is entitled to a judgment:

1. against Goldman Sachs on ACA's first and second causes of action, awarding ACA compensatory damages in an amount to be determined at trial of at least $30 million;

2. against Goldman Sachs on ACA's first and second causes of action, awarding ACA punitive damages in an amount to be determined at trial of at least $90 million;

3. against Paulson & Co. and Paulson Credit Opportunities on ACA's third, fourth and fifth causes of action, awarding ACA compensatory damages in an amount to be determined at trial of at least $30 million;

4. against Paulson & Co. and Paulson Credit Opportunities on ACA's third, fourth and fifth causes of action, awarding ACA punitive damages in an amount to be determined at trial of at least $90 million;

5. against Paulson & Co. and Paulson Credit Opportunities on ACA's sixth cause of action, awarding ACA the amount by which Paulson was unjustly enriched in an amount to be determined at trial;

6. interest, costs and expenses incurred in this action; and

7. such other and further relief as the Court deems just and proper.

Dated: New York, New York
January _, 2013

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